

**MEASURE A – STRONG SCHOOLS BOND OF
PALO ALTO UNIFIED SCHOOL DISTRICT**

AUDIT REPORT

**For the Fiscal Year Ended
June 30, 2009**

**MEASURE A – STRONG SCHOOLS BOND
OF PALO ALTO UNIFIED SCHOOL DISTRICT
AUDIT REPORT
For the Fiscal Year Ended June 30, 2009
Table of Contents**

	<u>Page</u>
Introduction and Citizens’ Oversight Committee Member Listing.....	1
Independent Auditors’ Report.....	2
FINANCIAL SECTION	
Balance Sheet.....	4
Statement of Revenues, Expenditures and Changes in Fund Balance	5
Notes to Financial Statements.....	6
OTHER INDEPENDENT AUDITORS’ REPORTS	
Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>	12
Independent Auditors’ Report on Performance.....	14
FINDINGS AND RESPONSES SECTION	
Schedule of Findings and Responses.....	18

**MEASURE A – STRONG SCHOOLS BOND
OF PALO ALTO UNIFIED SCHOOL DISTRICT
Introduction and Citizens’ Oversight Committee Member Listing
June 30, 2009**

The Palo Alto Unified School District (the “District”) was founded on March 20, 1893 under the laws of the State of California. This District operates under a locally elected five-member Board form of government and provides educational services to grades K – 12 as mandated by the State and Federal agencies. The District operates twelve elementary, three middle, two high schools, an adult education program, a Young Fives program and two children’s centers.

In June 2008, the voters of Santa Clara County approved by more than the required 55% favorable vote the Measure A – Strong Schools Bond (“Measure A”), authorizing the issuance and sale of general obligation bonds, not to exceed \$378,000,000. The Measure A – Strong Schools Bond is a Proposition 39 bond. The passage of Proposition 39 in November 2000 amended the California Constitution to include accountability provisions. Specifically, the District must conduct an annual independent performance audit to ensure that funds have been expended only on the specific projects listed in the full text of the Measure A – Strong Schools Bond ballot measure as well as an annual, independent financial audit of the proceeds from the sale of the bonds until all of the proceeds have been expended for bond-designated facilities projects.

Measure A bonds were issued by the District, through the County of Santa Clara. On August 27, 2008, Series 2008 of the Measure A bond authorization was issued, which consisted of current interest and capital appreciation bonds with an initial par amount of \$119,999,249 with stated interest rates of 2.50% to 5.50% and maturing through August 1, 2033. As of June 30, 2009, the principal balance outstanding on the Measure A Series 2008 bonds, excluding accreted interest to date, was \$119,999,249.

Upon passage of Proposition 39, an accompanying piece of legislation, AB 1908 (Chapter 44, Statutes of 2000), was also enacted, which amended the Education Code to establish additional procedures which must be followed if a District seeks approval of a bond measure pursuant to the 55% majority authorized in Measure A including formation, composition and purpose of the Citizens’ Oversight Committee, and authorization for injunctive relief against the improper expenditure of bond revenues.

The Citizens’ Oversight Committee was comprised of the following members as of June 30, 2009:

Name	Title	Representation
Mr. Ray Bacchetti	Chair	Senior Citizens’ Organization & Taxpayers’ Organization
Mr. Scott L. Darling	Vice Chair	At-Large Member
Mr. Gary W. Hornbeek	Member	Parent & PTA Organization
Mr. Deepak Kanungo	Member	Parent
Ms. Caroline Maser	Member	Parent
Mr. Jim McFall	Member	Business Organization
Mr. Steve Shevick	Member	Parent



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Measure A Citizens' Oversight Committee and
Governing Board Members of
Palo Alto Unified School District
Palo Alto, California

INDEPENDENT AUDITORS' REPORT

We have audited the accompanying balance sheet of the Measure A – Strong Schools Bond of Palo Alto Unified School District (the "District") as of June 30, 2009, and the related statement of revenues, expenditures and changes in fund balance for the fiscal year ended June 30, 2009. These financial statements are the responsibility of the District's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Note 1A, the financial statements present only the individual Measure A – Strong Schools Bond ("Measure A"), consisting of the net construction proceeds of Measure A Series 2008 general obligation bonds as issued by the District, through the County of Santa Clara, and are not intended to present fairly the financial position of the District in conformity with generally accepted accounting principles.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Measure A – Strong Schools Bond of Palo Alto Unified School District as of June 30, 2009, and the results of its operations for the fiscal year ended June 30, 2009, in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated September 10, 2009, on our consideration of Palo Alto Unified School District's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, grants agreements and other matters. The purpose of that report is to describe the scope of our testing of internal controls over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

A handwritten signature in cursive script that reads "Nigro Nigro & White, PC".

San Diego, California
September 10, 2009

Financial Section

**MEASURE A – STRONG SCHOOLS BOND
OF PALO ALTO UNIFIED SCHOOL DISTRICT
Balance Sheet
June 30, 2009**

ASSETS

Cash in county treasury	\$	114,049,280
Accounts receivable		<u>460,396</u>

Total Assets	\$	<u>114,509,676</u>
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LIABILITIES AND FUND BALANCE

Liabilities

Accounts payable	\$	<u>2,353,633</u>
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Total Liabilities		<u>2,353,633</u>
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Fund Balance

Unreserved		<u>112,156,043</u>
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Total Liabilities and Fund Balance	\$	<u>114,509,676</u>
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The accompanying notes to financial statements are an integral part of this statement.

**MEASURE A – STRONG SCHOOLS BOND
OF PALO ALTO UNIFIED SCHOOL DISTRICT
Statement of Revenues, Expenditures and Changes in Fund Balance
For the Fiscal Year Ended June 30, 2009**

REVENUES	
Interest income	\$ 2,187,573
Total Revenues	<u>2,187,573</u>
EXPENDITURES	
Facilities acquisition and construction	10,030,779
Bond issuance costs	1,583,200
Total Expenditures	<u>11,613,979</u>
Excess (Deficiency) of Revenues Over (Under) Expenditures	<u>(9,426,406)</u>
OTHER FINANCING SOURCES	
Proceeds from long-term debt	119,999,249
Premiums on bond issuance	1,583,200
Total Other Financing Sources	<u>121,582,449</u>
Net Change in Fund Balance	112,156,043
Fund Balance, July 1, 2008	<u>-</u>
Fund Balance, June 30, 2009	<u><u>\$ 112,156,043</u></u>

The accompanying notes to financial statements are an integral part of this statement.

**MEASURE A – STRONG SCHOOLS BOND
OF PALO ALTO UNIFIED SCHOOL DISTRICT**
Notes to Financial Statements
June 30, 2009

NOTE 1 – SIGNIFICANT ACCOUNTING POLICIES

A. Reporting Entity

The Palo Alto Unified School District was founded on March 20, 1893 under the laws of the State of California. This District operates under a locally elected five-member Board form of government and provides educational services to grades K – 12 as mandated by the State and Federal agencies. The District operates twelve elementary, three middle, two high schools, an adult education program, a Young Fives program and two children’s centers.

On June 3, 2008 the District voters authorized \$378 million in General Obligation Bonds (Measure A – Strong Schools Bond) to provide safe and modern schools; accommodate enrollment growth; upgrade aging classrooms, libraries, computer and science labs; repair or replace roofs, plumbing, heating, ventilation and electrical systems; improve fire alarms and school security; meet current earthquake standards; provide current technology; and replace old portables with permanent classrooms.

An advisory committee to the District’s Governing Board and Superintendent, called the Measure A – Strong Schools Bond (“Measure A”) Citizens’ Oversight Committee (“COC”) was established pursuant to the requirements of State law and the provisions of Measure A. The purpose of the COC is to inform the public concerning the expenditure of bond revenues. The COC is required by state law to actively review and report on the proper expenditure of taxpayers’ money for school construction. The COC provides oversight and advises the public whether the District is spending the Measure A – Strong Schools Bond funds for school capital improvements within the scope of projects outlined in the Measure A – Strong Schools Bond Project List. In fulfilling its duties, the COC reviews, among other things, the District’s annual performance and financial audits of Measure A activity.

The statements presented are for the individual Measure A – Strong Schools Bond of the District, consisting of the net construction proceeds of Measure A Series 2008 general obligation bonds as issued by the District, through the County of Santa Clara, and are not intended to be a complete presentation of the District’s financial position or results of operations.

B. Accounting Policies

The District accounts for its financial transactions in accordance with the policies and procedures of the California Department of Education’s *California School Accounting Manual*. The accounting policies of the District conform to generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB) and the American Institute of Certified Public Accountants (AICPA).

**MEASURE A – STRONG SCHOOLS BOND
OF PALO ALTO UNIFIED SCHOOL DISTRICT**
Notes to Financial Statements
June 30, 2009

NOTE 1 – SIGNIFICANT ACCOUNTING POLICIES (continued)

C. Basis of Accounting

Basis of accounting refers to when revenues and expenditures are recognized in the accounts and reported in the financial statements. Basis of accounting relates to the timing of measurement made, regardless of the measurement focus applied.

The financial statements are presented on the modified accrual basis of accounting. Under the modified accrual basis of accounting, revenues are recorded when susceptible to accrual; i.e., both measurable and available. "Available" means collectible within the current period or within 60 days after year-end. Expenditures are generally recognized under the modified accrual basis of accounting when the related liability is incurred.

D. Encumbrances

Encumbrance accounting is used in all budgeted funds to reserve portions of applicable appropriations for which commitments have been made. Encumbrances are recorded for purchase orders, contracts, and other commitments when they are written. Encumbrances are liquidated when the commitments are paid.

E. Deposits and Investments

In accordance with Education Code Sections 15357 and 41001, the District maintains a portion of its cash in the Santa Clara County Treasury. The county pools these funds with those of other districts in the county and invests the cash. These pooled funds are carried at cost, which approximates market value. Interest earned is deposited quarterly into participating funds. Any investment losses are proportionately shared by all funds in the pool.

F. Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenditures during the reporting period. Actual results could differ from those estimates.

**MEASURE A – STRONG SCHOOLS BOND
OF PALO ALTO UNIFIED SCHOOL DISTRICT
Notes to Financial Statements
June 30, 2009**

NOTE 1 – SIGNIFICANT ACCOUNTING POLICIES (continued)

G. Budgets and Budgetary Accounting

Annual budgets are adopted on a basis consistent with generally accepted accounting principles for all government funds. By state law, the District's governing board must adopt a budget no later than July 1. A public hearing must be conducted to receive comments prior to adoption. The District's governing board satisfied these requirements.

These budgets are revised by the District's governing board during the year to give consideration to unanticipated income and expenditures. Formal budgetary integration was employed as a management control device during the year for all budgeted funds. The District employs budget control by minor object and by individual appropriation accounts. Expenditures cannot legally exceed appropriations by major object account.

NOTE 2 – CASH AND INVESTMENTS

Summary of Cash and Investments

Cash and investments as of June 30, 2009 are classified in the accompanying financial statements as cash in county treasury for \$114,049,280.

Policies and Practices

The District is authorized under California Government Code to make direct investments in local agency bonds, notes, or warrants within the State; U.S. Treasury instruments; registered State warrants or treasury notes; securities of the U.S. Government, or its agencies; bankers acceptances; commercial paper; certificates of deposit placed with commercial banks and/or savings and loan companies; repurchase or reverse repurchase agreements; medium term corporate notes; shares of beneficial interest issued by diversified management companies, certificates of participation, obligations with first priority security; and collateralized mortgage obligations. Investments of debt proceeds held by trustees are governed by the provisions of debt agreements rather than the general provisions of the California Government Code. These provisions allow for the acquisition of investment agreements with maturities up to 30 years.

Cash in County Treasury – The District is considered to be an involuntary participant in an external investment pool as the District is required to deposit all receipts and collections of monies with their County Treasurer (Education Code Section 41001). The fair value of the District's investment in the pool is reported in the accounting financial statements at amounts based upon the District's pro-rata share of the fair value provided by the County Treasurer for the entire portfolio (in relation to the amortized cost of that portfolio). The balance available for withdrawal is based on the accounting records maintained by the County Treasurer, which is recorded on the amortized cost basis.

**MEASURE A – STRONG SCHOOLS BOND
OF PALO ALTO UNIFIED SCHOOL DISTRICT
Notes to Financial Statements
June 30, 2009**

NOTE 2 – CASH AND INVESTMENTS (continued)

General Authorizations

Except for investments by trustees of debt proceeds, the authority to invest District funds deposited with the county treasury is delegated to the County Treasurer and Tax Collector. The table below identifies some of the investment types permitted in the investment policy:

<u>Authorized Investment Type</u>	<u>Maximum Remaining Maturity</u>	<u>Maximum Percentage of Portfolio</u>	<u>Maximum Investment in One Issuer</u>
Local Agency Bonds, Notes, Warrants	5 years	None	None
Registered State Bonds, Notes, Warrants	5 years	None	None
U.S. Treasury Obligations	5 years	None	None
U.S. Agency Securities	5 years	None	None
Banker's Acceptance	180 days	40%	30%
Commercial Paper	270 days	25%	10%
Negotiable Certificates of Deposit	5 years	30%	None
Repurchase Agreements	1 year	None	None
Reverse Repurchase Agreements	92 days	20% of base	None
Medium-Term Corporate Notes	5 years	30%	None
Mutual Funds	N/A	20%	10%
Money Market Mutual Funds	N/A	20%	10%
Mortgage Pass-Through Securities	5 years	20%	None
County Pooled Investment Funds	N/A	None	None
Local Agency Investment Fund (LAIF)	N/A	None	None
Joint Powers Authority Pools	N/A	None	None

Limitations as they relate to interest rate risk, credit risk, and concentration of credit risk are described below:

Interest Rate Risk

Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. The District manages its exposure to interest rate risk by investing in the County Treasury. The District maintains an investment with the Santa Clara County Investment Pool with a fair value of approximately \$114,488,694 and an amortized book value of \$114,049,280. The weighted average maturity for this pool as of June 30, 2009 is 298 days.

**MEASURE A – STRONG SCHOOLS BOND
OF PALO ALTO UNIFIED SCHOOL DISTRICT
Notes to Financial Statements
June 30, 2009**

NOTE 2 – CASH AND INVESTMENTS (continued)

Credit Risk

Credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. Per County investment policy, the investments within the Santa Clara County Investment Pool are rated A3 or higher by Moody's Investors Service.

Concentration of Credit Risk

The investment policy of the District contains no limitations on the amount that can be invested in any one issuer beyond the amount stipulated by the California Government Code. District investments that are greater than 5 percent of total investments are in either an external investment pool or mutual funds and are therefore exempt.

NOTE 3 – ACCOUNTS RECEIVABLE

Accounts receivable as of June 30, 2009 consist of interest earned on the District's investment in the County Treasury.

NOTE 4 – CONSTRUCTION COMMITMENTS

The Measure A - Strong Schools Bond had construction commitments of \$2,651,061 as of June 30, 2009.

NOTE 5 – MEASURE A – STRONG SCHOOLS BOND GENERAL OBLIGATION BONDS

As of June 30, 2009, the principal balance outstanding on the District's Measure A – Strong Schools Bond ("Measure A") Series 2008 general obligation bonds, including accreted interest to date, was \$122,224,834.

- On August 27, 2008, Series 2008 bonds of the Measure A bond authorization were issued, which consisted of current interest and capital appreciation bonds with an initial par amount of \$119,999,249 with stated interest rates of 2.50% to 5.50% and maturing through August 1, 2033.

**MEASURE A – STRONG SCHOOLS BOND
OF PALO ALTO UNIFIED SCHOOL DISTRICT
Notes to Financial Statements
June 30, 2009**

NOTE 5 – MEASURE A – STRONG SCHOOLS BOND GENERAL OBLIGATION BONDS (continued)

The annual requirements to amortize all Measure A Series 2008 general obligation bonds payable outstanding as of June 30, 2009, are as follows:

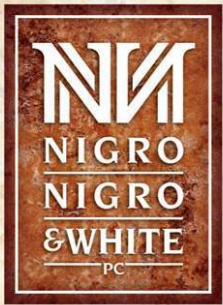
Fiscal Year	Principal (including accreted interest to date)	Accreted Interest	Current Interest to Maturity	Total
2009-10	\$ -	\$ -	\$ 252,911	\$ 252,911
2010-11	825,000	-	284,525	1,109,525
2011-12	1,780,000	-	263,900	2,043,900
2012-13	2,825,000	-	219,400	3,044,400
2013-14	2,350,000	-	148,775	2,498,775
2015-2019	14,808,219	5,941,781	84,150	20,834,150
2020-2024	28,823,083	26,761,917	-	55,585,000
2025-2029	38,548,842	56,961,158	-	95,510,000
2030-2034	32,264,690	76,560,310	-	108,825,000
Total	<u>\$ 122,224,834</u>	<u>\$ 166,225,166</u>	<u>\$ 1,253,661</u>	<u>\$ 289,703,661</u>

NOTE 6 – MEASURE A – STRONG SCHOOLS BOND EXPENDITURES BY PROJECT

The following table presents the expenditure amounts by project for the fiscal year ended June 30, 2009:

Project	Amount
Garland Elementary School	\$ 182,517
Ohlone Elementary School	199,208
Other elementary schools	80,460
J.L.S. Middle School	128,689
Jordan Middle School	67,055
Terman Middle School	13,386
Gunn High School	6,395,040
Palo Alto High School	428,576
Technology	1,544,932
Program administration - District	366,442
Program management services - unallocated	624,474
Series 2008 bond issuance costs	1,583,200
TOTAL	<u><u>\$ 11,613,979</u></u>

Other Independent Auditors' Reports



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Measure A Citizens' Oversight Committee and
Governing Board Members of
Palo Alto Unified School District
Palo Alto, California

**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING
AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN
AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE
WITH GOVERNMENT AUDITING STANDARDS**

We have audited the financial statements of the Measure A – Strong Schools Bond of Palo Alto Unified School District as of and for the fiscal year ended June 30, 2009, and have issued our report thereon dated September 10, 2009. We conducted our audit in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Palo Alto Unified School District's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Palo Alto Unified School District's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Palo Alto Unified School District's internal control over financial reporting.

A *control deficiency* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiency described in the accompanying schedule of findings and responses as finding #2009-1 to be a significant deficiency in internal control over financial reporting.

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A *material weakness* is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we do not believe that the significant deficiency described above is a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Measure A – Strong Schools Bond of Palo Alto Unified School District's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying schedule of findings and responses as item #2009-3.

Palo Alto Unified School District's responses to the findings identified in our audit are described in the accompanying schedule of findings and responses. We did not audit Palo Alto Unified School District's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the Measure A – Strong Schools Bond Citizens' Oversight Committee, the District's Governing Board, management, and the taxpayers of Palo Alto Unified School District and is not intended to be and should not be used by anyone other than these specified parties.



San Diego, California
September 10, 2009



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Palo Alto, California

INDEPENDENT AUDITORS' REPORT ON PERFORMANCE

We have audited the financial statements of the Measure A – Strong Schools Bond of the Palo Alto Unified School District (the “District”) as of and for the fiscal year ended June 30, 2009 and have issued our report thereon dated September 10, 2009. Our audit was made in accordance with generally accepted auditing standards in the United States of America and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

In connection with our performance audit, we performed an audit for compliance as required in the performance requirements for the Measure A – Strong Schools Bond (“Measure A”) for the fiscal year ended June 30, 2009. The objective of the audit of compliance applicable to the District is to determine with reasonable assurance that:

- The proceeds from the sale of the Measure A – Strong Schools Bonds were only used for the purposes set forth in the ballot measure and not for any other purpose, such as teacher and administrative salaries.
- The Governing Board of the District, in establishing the approved projects set forth in the ballot measure, evaluated the remodeling, new construction and renovations of items which will improve learning and to accommodate growth in the District, with no funds expended on administrator salaries.

In performing our audit of compliance, we performed procedures including but not limited to those listed as follows:

Internal Control Evaluation

Procedures Performed:

Inquiries were made of management regarding internal controls to:

- Prevent fraud or abuse regarding Measure A projects
- Ensure adequate separation of duties exists in the accounting for Measure A funds
- Prevent material misstatements in the financial statements
- Ensure expenditures are allocated to the proper fund(s)

We then performed substantive tests of financial statement balances to determine whether the controls designed by management were operating effectively, and to provide reasonable assurance that the fiscal year 2008-09 financial statement balances for the Measure A – Strong Schools Bond are not materially misstated.

Results of Procedures Performed:

The results of our audits tests show that internal control procedures appear to be working to meet the financial and compliance objectives required by generally accepted accounting standards and applicable laws and regulations, except as noted in the accompanying schedule of findings and responses as finding #2009-1. An unqualified opinion was expressed on the financial statements.

Facilities Site Walk

Procedures Performed:

We performed a site walk to verify that Measure A funds expended for the fiscal year ended June 30, 2009 were for valid facilities acquisition and construction purposes. NNW toured four District construction sites where 2008-09 construction work occurred: the Gunn HS Aquatic Center, the Gunn HS Industrial Arts Building, the J.L.S. Middle modular buildings, and the Jordan Middle modular building.

Results of Procedures Performed:

The Gunn HS Aquatic Center appeared to be complete, except for a shade canopy that was not yet installed as of September 1, 2009. The Gunn HS Industrial Arts building was undergoing substantial reconstruction with respect to its roofing, interior wiring, HVAC system, and interior framing. The J.L.S. and Jordan Middle modular buildings were installed as of the date of our audit.

Tests of Expenditures

Procedures Performed:

The following performance tests of expenditures were performed:

1. We tested expenditures to determine whether Measure A – Strong Schools Bond funds were spent solely on voter and Board approved school facilities projects (as set forth in the District’s Facilities Master Plan and the Measure A ballot measure language). The expenditure test included a sample of 70 payments, of which 59 were vendor payments and 11 were payroll payments, totaling \$6.4 million, or 55% of total expenditures for fiscal year 2008-09.
2. We also tested payments made to Gilbane Building Company and O’Connor Construction Management, the Measure A – Strong Schools Bond construction management and program management firms, respectively. We obtained the contracts for these firms and ensured that position rates per contract were accurately billed to the District.

Results of Procedures Performed:

We found the expenditures tested to be in compliance with the terms of the Measure A – Strong Schools Bond ballot measure and applicable State laws and regulations without exception.

Test of Contracts and Bid Procedures

Procedures Performed:

For the fiscal year ended June 30, 2009, NNW performed testing of 4 contracts to determine compliance with District policy and Public Contract Code provisions related to contracting and bidding:

- Project: Gunn High School Aquatic Center, Construction
Original Contract Award Amount: \$3,898,873
- Project: Gunn High School Aquatic Center, Landscaping
Original Contract Award Amount: \$39,000
- Project: Gunn High School Industrial Arts Building, Construction
Original Contract Award Amount: \$3,490,000
- Project: J.L.S. Middle School Modular Buildings Installation
Original Contract Award Amount: \$127,031

Test of Contracts and Bid Procedures (continued)

Results of Procedures Performed:

We found that the contracts tested followed proper bidding procedures, and were awarded in all cases to the lowest responsible bidder, except for the instance of noncompliance as described in the accompanying schedule of findings and responses as item #2009-3.

Our audit of compliance made for the purposes set forth in the second and third paragraphs of this report above would not necessarily disclose all instances of noncompliance.

In our opinion, except for the instance of noncompliance as noted in the accompanying schedule of findings and responses as item #2009-3, the District complied with the compliance requirements for the Measure A – Strong Schools Bond as listed and tested above.

This report is intended solely for the information and use of the Measure A – Strong Schools Bond Citizens' Oversight Committee, the District's Governing Board, management, and the taxpayers of Palo Alto Unified School District and is not intended to be and should not be used by anyone other than these specified parties.



San Diego, California
September 10, 2009

Findings and Responses Section

**MEASURE A – STRONG SCHOOLS BOND
OF PALO ALTO UNIFIED SCHOOL DISTRICT
Schedule of Findings and Responses
For the Fiscal Year Ended June 30, 2009**

Finding #2009-1: Separation of Duties in the Business Services Department

Finding: The District’s Measure A – Strong Schools Bond (“Measure A”) accountant enters new construction vendors into the QSS financial system and pays construction vendors. The Measure A accountant makes all general ledger entries for the Measure A - Strong Schools Bond and performs monthly cash reconciliations. Although no improprieties were detected, this concentration of duties creates an opportunity for one individual to misappropriate Measure A assets without timely detection.

Recommendation: Adequate separation of duties should exist in the area of setting up vendors and paying vendors. It is recommended that the District assign the duty of setting up vendors to the purchasing department in order to better separate duties. This will minimize the possibility for one individual to misappropriate assets without timely detection.

District Response: The District, in this start up year, had only 0.5 FTE accountant assigned to the program. Additional staff is being added to cope with the increased volume of the program and the duties will be separated appropriately and with the advice of the auditor.

Finding #2009-2: Agreement Between Account-Ability and QSS Financial Reports

Finding: There are two systems being maintained in the District. The Account-Ability system is a management tool used by the construction staff to track information as it is entered. The County’s Quintessential School Systems (“QSS”) system is the District’s financial system. It was noted in our audit that the Account-Ability Consolidated Expenditure Reports have variances by school/project name as compared to the year-to-date Financial Summary Reports generated by the QSS financial system, due primarily to timing differences in data entry between the two systems. The Account-Ability Consolidated Expenditure Reports were used during the fiscal year ended June 30, 2009 on the District’s monthly reports as posted on the District’s website and reported to the Citizens’ Oversight Committee (“COC”).

Recommendation: We recommend that the Measure A – Strong Schools Bond program general ledger (QSS) data be presented on the District’s monthly reports and reported to the COC instead.

District Response: The District will use Measure A – Strong Schools Bond program general ledger QSS data for its monthly reports and reports to the COC.

**MEASURE A – STRONG SCHOOLS BOND
OF PALO ALTO UNIFIED SCHOOL DISTRICT
Schedule of Findings and Responses
For the Fiscal Year Ended June 30, 2009**

Finding #2009-3: Bidding and Contract Change Order Procedures

Finding: We found in our test of bidding that the J.L.S. Middle School modular building installation project that exceeded the District’s formal bid limit of \$100,000. This project should have been advertised for two consecutive weeks in a newspaper, but in this case the District followed informal bidding procedures for projects between \$25,000 and \$100,000 that do not require newspaper notices. The J.L.S. modular building installation project was awarded at an initial contract amount of \$127,031. Fifteen prospective bidders on the J.L.S. modular building installation project were notified about the project by fax, and five bids were submitted.

Also, in our test of contract change orders, it was determined that the Board authorizes bids, approves construction contracts, and pre-authorizes change orders to construction contracts not to exceed ten percent (10%) of the original contract amount. Due to the pre-authorization of change orders, the Board is not currently notified of individual construction contract change orders.

Recommendations: The District should follow formal bidding procedures, including the requirement to place notices calling for bids in the newspaper, when construction projects are expected to cost \$100,000 or more.

The District’s management should inform the Board about all individual construction contract change orders. This will augment compliance with Public Contract Code at Section 20118.4, and will improve the Board’s ability to monitor the Measure A – Strong Schools Bond program.

District Response: The number of modulars was increased, at site request, at the last minute, and so this increased the cost. The bid process should have been adjusted by the construction team, but wasn’t. District accounting staff will now verify for all bids that the appropriate process has been followed prior to processing.

We agree that Board oversight will be enhanced by having the Board affirmatively act to approve individual change orders. We will do that by placing a list of negotiated change orders on the Board consent agenda.